

Year 2004-Records and Anti-Records

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In the year 2004 Russian oil companies posted record oil production of 458.8 million tons, making 2004 the most “fruitful” in the last 30 years. However, the rate of growth in production slowed to 8.9 percent as opposed to 11 percent in 2003. Even record-high world oil prices could not nudge production higher. Among the key reasons for the declining rate of growth are depletion of traditional oil and gas producing regions, low-level investment in exploration of new fields and insufficient development of new territories. New highs in the rate of production growth are not expected until the start of development of new regions: Eastern Siberia, the Far East and the Russian continental shelf.

The vast majority of oil production was by the Russian majors, 420.99 million tons of oil. Joint ventures and other producers with a mixture of Russian capital and foreign investment produced 23.42 million tons of crude. During the same period Gazprom produced 12.01 million tons of oil. Producers operating under a production sharing agreement turned out 2.38 million tons of oil.

Gas production in Russia in 2004 was 633.95 billion cubic meters, 2.8 percent above the 2003 figure. In 2004 Gazprom produced 544.4 billion cubic meters, 0.8 percent above the 2003 level. (See Inset 1. “Gazprom in 2004.”) From January through December, Russian oil majors produced 44.87 billion cubic meters of gas. Other oil and gas producers recovered 44.37 billion cubic meters of gas compared to 35.67 billion cubic meters in 2003.

Oil exports and transit to countries beyond the CIS countries in 2004 (excluding deliveries from Russian refineries and re-export of Russian crude via CIS countries) were 203.65 million tons. Of this figure, exports of Russian crude were 182.16 million tons, 17.5 percent above the 2003 level. Oil transited through the Russian system totaled 21.49 million tons, including 17.81 million tons from Kazakhstan and 2.77 million tons from Azerbaijan.

Last year the Transneft pipeline system exported 175.75 million tons of Russian crude to all foreign countries, excluding CIS and Baltic states. Another 6.42 million tons of oil were exported without accessing the Transneft system. Russian producers delivered 40.28 million tons of oil to the CIS and the Baltic states in 2004. That figure compares to 37.53 million tons in 2003 for the same category. In 2004 Russian majors exported 163 million tons of oil, an increase of 16.26 percent over the previous year. Companies ranked as non-majors shipped 9.06 million tons of oil to countries beyond the CIS and the Baltic states via the Transneft system.

The leader in sea shipments within the Transneft system was Novorossiysk. It transported 49.05 million tons of oil. Primorsk shipped 44.59 million tons; Odessa, 8.99 million tons; Butinge, 6.82 million tons; Tuapse, 4.82 million tons; and the marine oil terminal Yuzhny, 1.91 million tons.

According to CDU TEK, refineries received 227.98 million tons of feedstock in 2004 compared to 217.3 in 2003. Refineries owned by oil companies and Gazprom processed 194.13 million tons of this feedstock, up from 188.4 million tons in 2003. The remaining oil, 33.82 million tons, was also exported. The Russian refining industry receives very limited investment, no more than 30 billion rubles per year from all sources. Inadequate investment prevents the refineries from improving the very low level of light oil products refining in Russia, which stands at only 73 percent.

In contrast to Russian oil production, Russian oil sector investment activity last year hit a sort of "anti-record." If in 2003 oil industry investments amounted to 225.9 billion rubles or \$8.1 billion, in 2004 they were only 167.1 billion rubles or \$6.0 billion. As Russian Federation Minister of Economic Development and Trade German Gref observed, the influence of high oil prices no longer give the boost expected to the Russian economy. GDP growth had been projected at 7.1 percent but was actually 6.8 percent. Investment growth for the entire Russian economy did not reach its projected level of 11.5 percent.

Against a Background of Price Jumps

Exactly one year ago Gref predicted that "In the next years development will take place under less favorable external conditions: lower prices for oil and continual strengthening of the national currency." (See "Setting Records," *Russian Petroleum Investor*, March '04.) The minister was wrong. In 2004 world oil prices not only did not go down, they hit highs previously unimaginable At its peak in October 2004,

RUSSIAN OIL & GAS SECTOR IN 2003-2004

Company	Oil Production, thousand tons		Gas Production, million cu meters		Russian Oil Exports via Transneft System, thousand tons		Oil Refining, thousand tons	
	2003	2004	2003	2004	2003	2004	2003	2004
YUKOS	80,747.00	85,678.50	3,447.80	3,425.80	29,632.10	34,047.10	30,633.30	31,541.60
LUKOIL	78,908.20	84,103.10	4,699.00	5,015.40	27,108.70	33,029.10	34,024.40	35,249.50
TNK-BP (inc. SIDANKO)	61,567.90	70,265.00	6,818.30	8,004.60	27,018.90	30,843.50	18,954.90	20,184.80
TNK	42,961.20	49,490.10	4,974.20	5,858.70	18,767.20	26,721.10	14,317.90	14,676.30
SIDANCO	18,606.70	20,774.90	1,844.10	2,145.90	8,251.70	4,122.40	4,637.00	5,508.50
Surgutneftegas	54,025.30	59,619.90	13,882.60	14,309.70	18,278.70	20,867.50	15,212.00	15,964.70
Sibneft	31,393.50	33,984.50	1,986.10	1,954.50	11,611.70	13,371.30	13,832.20	14,308.20
Tatneft	24,668.70	25,099.50	728.00	735.90	10,484.10	12,023.60		
Slavneft	18,095.20	22,009.30	822.50	918.40	5,814.70	8,182.50	11,708.50	12,429.90
Rosneft	19,570.30	21,599.90	7,017.50	9,377.10	6,388.60	6,764.00	9,528.60	9,349.80
Bashneft	12,046.10	12,031.80	368.50	360.90	3,861.30	3,861.30		
Oil Companies	383,007.50*	420,994.40*	40,435.40*	44,875.30*	140,198.80	162,989.90	133,893.90	139,028.50
Gazprom	10,020.60	12,008.50	54,172.30	544,418.90	217.10	457.00		
PSA Operators	2,101.60	2,382.40	174.80	291.80	728.30	707.30		
Other Producers	25,247.20	23,423.10	35,672.00	44,367.90	8,611.30	9,057.70	54,497.10**	55,105.80**
Total in Russia	421,377.00	458,808.40	616,454.50	633,953.80	169,512.60***	197,231.50***	188,391.00	194,134.30

Note:

*Including new vertically integrated company Russneft

**including such large refineries as Moscow Oil Refinery, Bashneftekhim, Salavatnefteorgsintez, Nizhnekamskneftekhim, Khabarovsk Oil Refinery and others

***Total export and transit via Transneft System

Source: RF Ministry of Industry and Energy

RUSSIAN MAJORS: INVESTMENT AND DRILLING IN 2003-2004					
Company	Investment, million rubles	Exploration Drilling, thousand meters	Development Drilling, thousand meters	Exploration Drilling, thousand meters	Development Drilling, thousand meters
	2004	2003		2004	
LUKOIL	36,095.70	1,073.40	125.30	1,028.90	94.90
YUKOS	18,670.70	1,180.90	43.10	747.00	20.70
Surgutneftegas	40,274.80	2,777.50	244.10	2,822.00	214.30
TNK (inc. SIDANKO)	19,623.00	531.10	21.90	772.60	39.90
Sibneft	12,295.10	687.80	50.60	804.30	14.20
Tatneft	7,776.40	602.50	48.20	504.60	47.60
Slavneft	6,350.80	251.80		284.50	19.20
Rosneft	18,049.90	483.20	39.10	468.10	38.80
Bashneft	6,654.30	333.90	70.90	364.50	43.10
Oil Companies	165,790.70	7,929.10*	643.20*	7,932.50*	540.70*
Total in Russian Oil Sector	167,094.60	8,576.20	680.50	8,413.70	583.30
<i>Note: *Including new vertically integrated company Russneft</i>					
<i>Source: RF Ministry of Industry and Energy</i>					

the Brent oil price was up 70 percent from the start of the year, and on average oil price growth was 40 percent for the year. However, both the minister and analysts were right that in 2004 Russia's rate of growth in oil production would decline, although their forecasts were based on an anticipated drop in oil price. Even though forecasted production growth was seven percent and the actual figure was about nine percent, the decelerating tendency is more that evident, leading to the question of why this taking place. Gennady Krasovsky, head of the Investor Relations Department of LUKOIL believes that the main cause for the industry's slower growth is that most companies operate in their traditional regions. Fields are depleted and production cannot be increased at earlier rates. Companies need to go to new regions. However, most companies have no new large fields or discoveries of which to boast.

Companies not only need new regions, they also have to intensify their exploratory work. (See "The Ministry of Natural Resources Reorients," *Russian Petroleum Investor*, January'05.) According to the Ministry of Natural Resources, the growth of reserves of liquid hydrocarbon reserves over the past five years offset only 85% of production amounts. According to Research Institute Oceanography VNII, investment in geological exploration in Russia equals no more than 0.3 percent of the revenue generated from hydrocarbon production.

Discovery of new fields and entry into new regions require huge investments. Over the next 15 years planned investments only in geological exploration alone are to increase to 1.78 trillion rubles (\$64 billion). Most of this planned funding, 90 percent, is supposed to come from non-government budget sources. According to specialists, if the required investment actually occurs, the gap between production and reserves growth will narrow to 98 percent by 2010. By 2012 these parameters would balance.

Minister of Natural Resources Yury Trutnev is displeased with this time frame. On the eve of the New Year all cabinet members of the Russian Federation published their goals for the coming year on the government's official website. Trutnev said: "In 2005 we plan to double the number of blocks put up for geological exploration. The federal budget will allocate 4.6 billion rubles for this work and, as a result, we plan to increase hydrocarbon reserves by 4.2 billion tons of fuel oil equivalent, including 2 billion tons for land fields."

There is hope that the rate of growth in production will stabilize. That hope rests mainly with the entry of Russian companies into new regions, particularly Eastern Siberia, the Far East and the Russia's continental shelf. The government's program for developing hydrocarbon resources of the

Northwestern Region to 2020 will also contribute toward exploration and production growth in the new territories. Of course, large-scale development of new territories will not begin in 2005, but as soon as it occurs production will rise.

Same Leaders, but Not for Long

The balance of power within the Russian oil and gas sector that has evolved over the last few years is going through a radical change. YUKOS led the list of top five producers in 2004. These top five accounted for 72.7 percent of Russian's production. In 2005 YUKOS will disappear, not only from this list but most likely from the Russian upstream sector. Membership in the future list remains unclear due to murkiness around the future of Yuganskneftegaz. Will Yuganskneftegaz become a part of Rosneft? Or Gazprom? What will become of YUKOS? It is clear that certain to be among the leaders are: LUKOIL, which in 2004 produced 84.1 million tons of oil, second to YUKOS; TNK-BP, 70.3 million tons; Surgutneftegaz, 59.6 million tons and Sibneft, 33.98 million tons. (See Chart 1. "Russian Oil and Gas sector in 2003-2004.")

A new company, which included Yuganskneftegaz's planned 2005 production of 54 million tons, could be either the last on the top five list, or take second place as a combination of Rosneft and Yuganskneftegaz, with production of 76 million - 78 million tons, or even come in first with production of 88 million - 92 million tons in the form of Gazprom plus Rosneft plus Yuganskneftegaz. Everything depends on how the production growth scenarios at Rosneft and Gazprom are played out. The situation with other YUKOS subsidiaries is similarly unclear; they too may change ownership. These subsidiaries account for another 30 million tons of oil annually, a sum sufficient to affect the leadership positions.

Division of the playing field at the top may also be affected by TNK-BP's corporate restructuring. (See Inset 2. "TNK Changes Structure and Legal Residence.") By consolidating the commodity flows of its subsidiaries ONAKO and Sidanco, TNK-BP was able to report production of slightly more than 70 million tons to place third on the top five list. Bearing in mind that TNK-BP and Sibneft acquired Slavneft jointly, TNK-BP controls at least 50 percent of Slavneft's production. That is 11 million tons of oil per year. Therefore, it is clear that in 2004 TNK-BP produced or controlled production of 81 million tons of oil. While this does not bring TNK-BP higher than third

RUSSIAN MAJORS: WELLS IN 2003-2004

Company	Oil & Gas Wells					
	Total, units	Idle wells, %	New wells*, units	Total, units	Idle wells, %	New wells*, units
	1.01.2004			1.01.2005		
LUKOIL	27,508.00	18.30	475.00	56,502.00	17.90	485.00
YUKOS	17,801.00	31.10	391.00	17,366.00	26.10	281.00
Surgutneftegas	16,960.00	12.60	1,136.00	16,719.00	11.90	887.00
TNK	16,178.00	41.60	150.00	17,597.00	43.30	228.00
SIDANCO	8,124.00	30.60	43.00	8,152.00	33.80	86.00
Sibneft	7,995.00	56.50	218.00	8,099.00	57.30	216.00
Tatneft	21,517.00	14.50	443.00	21,682.00	18.00	463.00
Slavneft	3,963.00	16.20	88.00	3,978.00	19.10	87.00
Rosneft	8,868.00	6.80	197.00	8,529.00	6.70	180.00
Bashneft	18,537.00	18.80	230.00	18,600.00	17.20	187.00
Oil Companies	148,885.00**	28.40**	3,377.00**	151,308.00**	23.80**	3,220.00**
Total in Russian Oil Sector	155,286.00	23.40	n/a	155,671.00	23.60	3,529.00

Note: *Wells in development and exploration drilling

**Including new vertically integrated company Russneft

Source: RF Ministry of Industry and Energy

place in 2004, if Yuganskneftegaz assets are not included under Rosneft or Gazprom in 2005, and if TNK-BP and Sibneft settle the situation with Slavneft, TNK may place second to LUKOIL in the 2005 list.

The rate of growth in hydrocarbon production is another factor influencing rank among the leading oil companies. It was precisely this element that enabled YUKOS to occupy the first position on the list, long LUKOIL's domain. In 2004 the leaders in production growth were Slavneft (21.63 percent) and TNK-BP (14.1 percent), including Slavneft, jointly owned with Sibneft. By itself Sibneft registered only eight percent growth. Surgutneftegaz and Rosneft reported approximately ten percent production growth each. LUKOIL and YUKOS showed growth of about six percent. Tatneft increased its production by about two percent and Bashneft held its production at the 2003 level.

It is worth mentioning that the Russian oil and gas community doubts that it will be possible to have production growth of from 15 percent - 20 percent yearly from the fields of Western Siberia. This is because companies have followed a policy of selective production: the most highly productive deposits are developed first while the difficult to recover deposits that may comprise up to 90 percent remain in the ground. It is likely that the Ministry of Natural Resources will impose stricter production requirements to promote more comprehensive oil recovery.

In contrast to low rates of increase of production, companies significantly increased oil exports. Again the leader by a wide margin was Slavneft. That company exported 40.7 percent more oil than in 2003. LUKOIL increased oil exports by 21.8 percent. YUKOS, TNK-BP, Sibneft, Tatneft, Surgutneftegaz all demonstrated 14 percent -15 percent export growth. Only Rosneft reported remarkably low growth of six percent.

Insofar as natural gas production by oil companies is concerned, the two traditional leaders in associated gas extraction, Surgutneftegaz (14.3 billion cubic meters) and Rosneft (9.37 billion cubic meters) were joined by TNK-BP which placed third in 2005 with eight billion cubic meters of gas.

Lessons from YUKOS

The YUKOS case did not pass unnoticed by the Russian oil majors. As Russian journalists have written, companies suddenly started to like paying taxes. According to the investment company Aton, Sibneft's net profit for the first nine months of 2004 was 34.8 billion rubles, approximately \$1.24 billion. Progress is undeniable, especially when compared with the same period of 2003 when the company reported losses of 732 million rubles. And Sibneft's pre-tax profit grew 88-fold while the price of oil increased only 40 percent! Sibneft's share of profit paid in taxes to the state grew from seven percent in 2003 to 25 percent in 2004. While less dramatic than Sibneft, other companies increased the share of tax paid from their 2004 profit: LUKOIL to 25.2 percent over the previous year's 24 percent, TNK-BP to 16.5 percent from 7.5 percent, Surgutneftegaz to 22 percent from 19 percent.

Now, when energy prices are rising, the government is paying closer attention to company activities and maximally increases the tax burden on the energy industry. In the last three years oil export duties more than tripled. The rate of tax on production of mineral resources (TPMR) was also increased. The stabilization fund of Russia, which receives funds attributable to the rise in the price of oil, grew from 106 billion rubles to 564.8 billion rubles. The base amount of 500 billion rubles in the fund is not to be spent. Gref has suggested that the remaining funds could wisely be employed to realize oil and gas projects.

On January 1, 2005, amendments to Chapter 26 of the Tax Code of the Russian Federation "Tax on Production of Mineral Resources" (TPMR) come into force. Along with these amendments has

come an increase in the rate of this tax. In accordance with the amendments, the TPMR rate increases from 347 rubles per ton to 419 rubles per ton. (See "The Russian Paradox," *Russian Petroleum Investor*, February'05.) "What will happen next is yet unclear and it will become [clear] already the next year [2005]. It may be that we will abandon this formula and switch to ad-valorem rate and will [charge] as for all other kinds of mineral resources except natural gas. Or, possibly we would have to extend the use of the formula for a certain period, for one, two or three years," said Alexander Ivaneyev, deputy head of the Department for Tax and Customs and Tariffs Policy at the Ministry of Finance.

In 2005 Russia will completely switch to levying indirect taxes on exports, VAT and excise taxes, on the principle of tax payment in accord with the destination country. Russian companies exporting oil and gas to CIS countries before 2005 had paid VAT to Russia. Now they will pay this tax to the budgets of the countries of destination. Estimates are that this will cost the Russian budget about \$800 million of revenue in 2005. Oil companies unanimously contend that this gap will have to be filled by Russian companies, and in the end by Russian residents.

Possibly the only positive change in the tax regime for oil companies is the reduction in oil export duty, effective February 1, 2005. The duty will be \$83 per ton compared with the record-high duty of \$101 per ton previously in place. The duty on oil exports from Russia will be reevaluated every two months based on two-month price monitoring for Russian crude in world markets. The duty set as of February 1 is based on Russian crude price data for November-December 2004. The average price of Russian crude for that period was \$36.36 per barrel compared to \$40.14 per barrel in September-October; this drop provided the grounds for reduction in export duty.

Oil companies are resigned to the idea that taxes must be paid in full. It is more difficult for them to dispell their fear of further re-distribution of oil and gas sector assets and the possibility cannot be excluded.

The second lesson from the YUKOS case is that oil companies must "make friends" with the state and demonstrate their loyalty to the government. This concerns large mergers and acquisitions, entry into new regions, extending guarantees for future government transportation and export routes and many, many other areas where the paths of oil and gas companies and government cross. They cross very often. □

Gazprom in 2004

Gazprom, according to company managers, showed good results in the past year. "Results of our work clearly demonstrate that Gazprom is an effective and rapidly developing gas company with a stable financial position and great potential for future growth," notes the company's press release. The statement is supported with figures: Gas production grew by 4.9 billion cubic meters over production in 2003; the total in 2004 was 545.1 billion cubic meters.

Production of oil and gas condensate in 2004 also increased, reaching 12 million tons. This figure exceeds 2003 production by one million tons. In 2004 the company processed 32.4 billion cubic meters of gas and 11.3 million tons of oil and gas condensate. Gas-processing plants produced 5.2 million tons of sulfur, 2 million tons of gasoline, 1.7 million tons of diesel fuel, 1.85 tons of liquefied gas and 393,000 thousand tons of fuel oil.

Gas exports surpassed 190 billion cubic meters: The largest share, 140.5 billion cubic meters, was shipped to customers in distant countries, while 52.2 billion cubic meters were delivered to the CIS and Baltic states. These figures outstrip the previous year's exports to these regions by 7.6 and 9.6 billion cubic meters, respectively. In addition, Gazprom transported through its pipelines 60.2 billion cubic meters of gas produced by private Russian companies and 50.2 billion cubic meters of gas from Kazakhstan, Uzbekistan and Turkmenistan.

Export revenue from deliveries to Europe was estimated at \$19.2 billion, a record for Gazprom. The company reported growth in capitalization of 37 percent outside of the Russia Federation and 114 percent inside the country. With gas production higher by only 0.9 percent and exports revenues up by 16.4 percent, it is possible to draw certain conclusions. Namely, Gazprom's prosperity was the result of high gas prices, which reached \$150 per thousand cubic meters in the European markets during 2004. And the company's capitalization boom, experts say, was the response of the market to the government's promises to liberalize the market for trading Gazprom's shares.

"Gazprom's weak growth in industrial indicators," says Valery Nesterov analyst with investment company Troika Dialog, "is explained by the fact that giant fields have already been worked out and the recently-launched Zapolyarnoye project will only be able to compensate for the drop in production.

Oil companies and independent producers could increase their gas production at a much higher pace, but they are constrained by Gazprom's monopoly on exports, low gas prices in the domestic market and difficulties accessing gas transportation networks."

Analysts forecast that as early as 2008 Gazprom will confront problems implementing its production program. Reserves of its principle fields, including Medvezhye, Urengoiyskoye, Yamburgskoye, are declining. Today the company's greatest hope for further increases in gas production are the Yety-Purovskoye gas field and the Pestsovaya area of Urengoiyskoye gas-condensate field, both of which Gazprom began exploiting in 2004. Zapolyarnoye is another important field. It is currently producing at its design capacity of 100 billion cubic meters of gas per year.

Before launching production at these new large fields, Gazprom found a way to compensate for anticipated gas shortages. The company signed a contract to the purchase Turkmen gas through 2028. The contract's volume is 1.8 trillion cubic meters. Under the terms of this contract, in 2005 and 2006 Gazprom will purchase Turkmen gas at \$44 per thousand cubic meters; thereafter, the gas price will be pegged to the oil basket. This means that in the future Gazprom will have to pay more. Today, Turkmenistan is selling gas to Ukraine at \$58 per thousand cubic meters. There is also no guarantee that Turkmenistan will be able to supply natural gas at full volume. There has been no announcement of results of certification of the size of the reserves of the Dovletabad field gas from which gas is to be exported to Russia under this contract.

Gazprom's press service terms mineral resource base development as one of the company's priorities. Today growth in resources does not compensate for production, but the company plans to reach parity level in 2006. Gazprom's chief task in 2005 is to develop its gas transportation network and improve the system's reliability. Of a total investments budget of 212.6 billion rubles, 65 percent has been allocated to building of the transportation network.

TNK Changes Structure and Legal Residence

TNK-BP, a Russian-British company, currently registered in British Virgin Islands, announced that an independent valuation of its assets had been completed that will allow it to register a new holding company in Russia. The new holding company will be the profit center for the company. The valuation provides the basis upon which TNK-BP will offer minority shareholders in its subsidiaries an exchange of those share for shares in the new holding company.

TNK-BP President Robert Dudley identified the main goals of restructuring: to simplify corporate structure, to consolidate minority shareholders' interests in the TNK-BP companies, to improve transparency and efficiency of corporate governance. Financing to undertake the restructuring, according to TNK-BP Chief Financial Officer Kent Potter, may come from sources outside the company. The size of the borrowing will depend on the percentage of minority shareholders who decline the share exchange offer in preference for selling their TNK-BP subsidiary shares.

The share exchange will proceed in two stages. During the first stage of restructuring, the shares of TNK, ONAKO and Sidanco will be contributed to TNK-BP Holding. That company was registered in November 2004 in the Tyumen Region, in the settlement of Uvat. Subsequently, these entities will be liquidated. Then, shares of other TNK-BP companies, mainly subsidiaries of TNK, ONAKO and Sidanco will be contributed to the holding company. According to the independent valuation prepared by Deloitte Touche Tohmatsu, TNK-BP Holding's shareholder capital should be 517.8 billion rubles, of which Tyumen Oil Company (TNK) was valued at 292.5 billion rubles, ONAKO at 35.1 billion rubles and Sidanco at 160.1 billion rubles.

At an extraordinary shareholders' meeting on March 1, 2005, minority shareholders of TNK, ONAKO and Sidanco will vote on reorganization of these holdings in the form of merger with TNK-BP Holding. The shares of those voting in favor or abstaining will be converted to shares of TNK-BP Holding. The conversion ratio for TNK will be 2.66, for ONAKO – 1.89, for Sidanco – 23.49. Shareholders voting against reorganization will be able to sell their shares at the prices set in the Deloitte valuation:

- Price of one share of TNK will be 92.5 rubles;
- Price of one share of ONAKO will be 65.6 rubles;
- Price of one share of Sidanco will be 815.9 rubles.

If the offering price is not acceptable, minority shareholders may challenge the figures in court.

In Dudley's words, initially restructuring will only involve the contribution of ONAKO, TNK and Sidanco shares to TNK-BP Holding. "We do not plan to reassign to TNK-BP Holding our other companies – including RUSIA Petroleum, Slavneft, assets in Ukraine, the STBP Holdings' BP gasoline stations chain in Moscow," said Dudley.

Dudley clarified that at this time TNK-BP does not plan to consolidate Slavneft, owned on parity basis with Sibneft, as it is in the process of being divided by its stockowners. "When split-up is complete, and this will take considerable time, we, naturally, intend to make [these assets] a part of TNK-BP Holding. Currently, we are partitioning Slavneft's retail network. It is clear that production assets are especially important to Russia and therefore we started the division process with retail. At this moment no other options are being considered," said Dudley.

If everything goes as planned, during the spring months TNK-BP will complete the share buy-out from TNK, ONAKO and Sidanco shareholders. In the third quarter of 2005 TNK-BP Holding, including TNK, ONAKO, and Sidanco, will make an offer to minority shareholders of 14 operating subsidiaries to "voluntarily" swap their shares for TNK-BP Holding shares. This will be the second stage of restructuring. Minorities of these subsidiaries will not have the right to demand purchase of their shares as in the case of TNK, ONAKO and Sidanco. According to Dudley, if they refuse to swap for TNK-BP Holding's shares they will simply remain minority shareowners of the company's subsidiaries.